

**Management Advisory Report: Project  
Management Techniques Would Help in  
Managing Risks For the Increased Employee  
Plan Determination Letter Workload**

**May 2002**

**Reference Number: 2002-10-104**

**This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.**



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

May 30, 2002

MEMORANDUM FOR COMMISSIONER, TAX EXEMPT AND GOVERNMENT  
ENTITIES DIVISION

A handwritten signature in cursive script, reading "Pamela J. Gardiner".

FROM: Pamela J. Gardiner  
Deputy Inspector General for Audit

SUBJECT: Final Management Advisory Report: Project Management  
Techniques Would Help in Managing Risks For the Increased  
Employee Plan Determination Letter Workload  
(Audit # 200110050)

This report presents the results of our review of the Tax Exempt and Government Entities (TE/GE) Division's strategy for processing an anticipated higher number of employee plan determination letter applications. The overall objective of this review was to determine if potential risks to the implementation of the employee plans determination letter strategy are being effectively addressed by the TE/GE Division.

In summary, we found that the TE/GE Division designed a multifaceted strategy to address the challenge of continuing to provide top-quality service to all employee plan customers during the expected peak in the determination letter application workload. The strategy reflects a high level of commitment to minimizing any detrimental impact on customer satisfaction or customer burden that might be caused if the increased number of applications causes delays in processing determination requests. Timely responses are important. If the terms of a benefit plan are incomplete or incorrect, a prompt determination from the Internal Revenue Service (IRS) will enable the employer to make the necessary corrections as quickly as possible.

Although TE/GE management developed a strategy to prepare for the peak determination letter workload, we believe project management techniques should be used to effectively implement the determination letter strategy. The TE/GE Division's strategy did not include a structured project management approach to coordinate, monitor, or report on the actions in process by all the various functions involved with implementing the strategy. Instead, TE/GE management used conference calls and

status meetings to discuss the actions needed to prepare for the peak receipt period. This made it difficult to know whether the TE/GE Division would be ready to handle the increased workload when the peak period began, as well as to identify new risks as the strategy unfolds. A structured approach would help all levels of TE/GE management review what issues exist and assess whether associated risks have been addressed to their satisfaction.

Management's Response: TE/GE management agreed with our recommendation and appointed a manager to assume program responsibility and apply project management techniques for the increase in determination letter workload. Management's complete response to the draft report is included as Appendix IV.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendation. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

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**Background**

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Employer-sponsored employee benefit plans<sup>1</sup> must comply with numerous laws and regulations in order to qualify for favorable tax treatment of the plan's assets. Examples of favorable tax treatment for a plan that meets the qualification requirements include: the assets and income of the plan are tax-exempt, contributions to and expenses incurred by the plan are deductible, and participants are not taxed on their benefits until distributions are received from the plan.

Many employers want to know if, in the opinion of the Internal Revenue Service (IRS), the terms of their plans satisfy the qualification requirements. The IRS provides a way for employers to get such an assurance by means of the determination letter program. In the determination letter program, the IRS evaluates the employer's benefit plan to determine its compliance with the requirements. If the IRS identifies unacceptable features, the employer is given an opportunity to make appropriate modifications to the plan. When the format of a plan satisfies the applicable requirements, the IRS issues a favorable determination letter. While employers are not required to request a determination letter, a favorable letter gives the employer a reliance that the plan is qualified and that, as a result, it is entitled to favorable tax treatment as long as the plan is operated under the terms on which the letter was issued.<sup>2</sup>

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<sup>1</sup> Employee benefits plans include programs such as pension plans, profit-sharing plans, Internal Revenue Code 401(k) retirement plans, employee stock ownership plans, and stock bonus plans.

<sup>2</sup> The IRS also has an examination program that reviews selected employee plans to determine if they are actually operated in a qualified manner. Examinations are conducted on plans that both do, and do not, have a favorable determination letter. If operational compliance problems are found, sanctions are applied or the plan can lose its tax exempt status. There is also a self-correction program that allows employers to voluntarily identify plan defects and make appropriate corrections.

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A favorable determination letter is limited in scope<sup>3</sup> and may also have a limited useful life. In general, the IRS issues a determination letter based on the law in effect at the time the application for a determination was received. If there is a subsequent change in a statute, regulation, or revenue ruling applicable to the plan, the plan must be amended to comply with the new requirements and to maintain its qualified status. As a result, after modifying the plan, the employer would need to again ask for a determination letter to have reliance that the plan was properly redesigned.

The IRS allows plan sponsors time to incorporate tax law changes without any penalty or sanction. This is called the remedial amendment period. The end of the remedial period becomes a deadline for the timely filing of a determination letter application that relates to the changes in requirements.

Varying remedial periods can be set for different laws, types of amendments, or types of applications involved. The IRS can, and has, extended the remedial amendment period for certain statutes and consolidated several laws' provisions into one remedial period.

The ending of the remedial period for one group of tax law changes, which the IRS refers to as GUST,<sup>4</sup> was scheduled for December 31, 2001. Based on the likelihood that employers would ask for a determination letter on their revised benefit plans, the IRS estimated that the number of determination letter applications may quadruple during Fiscal Years (FY) 2002 and 2003 as compared to normal

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<sup>3</sup> See Favorable Determination Letter (Publication 794), for an explanation of the significance and limitations of a favorable determination letter.

<sup>4</sup> The Uruguay Round Agreements Act, Pub. L. 103-465; the Uniformed Services Employment and Reemployment Act of 1994, Pub. L. 103-353; the Small Business Job Protection Act of 1996, Pub. L. 104-188; the Taxpayer Relief Act of 1997, Pub. L. 105-34; the IRS Restructuring and Reform Act of 1998, Pub. L. 105-206; and the Community Renewal Tax Relief Act of 2000, Pub. L. 106-554 are collectively referred to as GUST.

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receipt levels.<sup>5</sup> The IRS has had other peak periods of receipts around 1995, 1986, and 1978.

On November 14, 2001, the IRS announced that as a result of the September 11, 2001, terrorist attack on the United States, the deadline for timely filing for many determination letter applicants (i.e., the beginning of the peak period) was extended. Depending on the type of employer plan, the end of the GUST remedial period was extended to February 28, 2002, or to alternate dates spread across Calendar Years 2002 and 2003 on a plan-by-plan basis.<sup>6</sup> Based on these revised dates and the fact that determination applications are voluntary, the actual number and timing of applications that will be received by the IRS is not certain.

We contacted personnel in the IRS Tax Exempt and Government Entities (TE/GE) Division and other IRS divisions in Cincinnati, Ohio, and Washington, D.C., between August 2001 and March 2002. The review was conducted in accordance with the President's Council on Integrity and Efficiency's *Quality Standards for Inspections*. Detailed information on our objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

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### **A Multifaceted Strategy Has Been Designed to Address the Expected Peak in the Employee Plan Determination Letter Workload**

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The TE/GE Division designed a multifaceted strategy to address the challenge of continuing to provide top-quality service to all employee plan customers during the expected peak in the determination letter application workload. This is prominently shown in the TE/GE Division's FY 2002-2003 Strategic Assessment, Strategic Plan, and Program Plan; as well as the FY 2001 Business Performance Review. General management techniques,

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<sup>5</sup> The FY 2001 volume of receipts was 30,492. At the end of FY 2001, the IRS estimated 145,000 receipts for FY 2002 and 117,000 for FY 2003. In December 2001, the FY 2002 estimate was reduced to a range of 110,000 to 120,000 receipts.

<sup>6</sup> The exact remedial expiration date depends on whether a plan is individually designed or is based on a model plan that has already been submitted for review. There are also varying disaster relief rules depending on the circumstances of the parties involved with a plan.

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such as defining operational priorities and improvement projects, are used at this level. Major components of the strategy include:

- Adding employees and other resources to the determination letter program to help process the higher number of applications.
- Using various customer education and outreach strategies to help employers understand and comply with the application process.
- Modifying procedures and forms to simplify the determination letter process, including allowing adopters of standardized and pre-approved model plans to obtain reliance without the need to request a determination letter.
- Identifying improvement projects to address information system issues that have an impact on the determination letter program.

The TE/GE Division's strategy reflects a high level of commitment to minimizing any detrimental impact on customer satisfaction or customer burden that might be caused if the increased number of applications causes delays in processing determination requests. For FY 2002, the TE/GE Division has given priority to the strategy within its Employee Plans (EP) function. For example, management is shifting a significant part<sup>7</sup> of the staff resources from the EP examination program to the EP determination program. These agents will be trained to review and process determination applications. Also, additional sites will be set up to screen the incoming applications. Normally, all determination letter applications are screened in one centralized location in order to separate those that could be given a favorable letter based on the merit of the documents

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<sup>7</sup> At the end of FY 2001, the TE/GE Division estimated that 186 staff years would be shifted from the EP examination program to the determination program in FY 2002. That amount would represent about 44 percent of the 418 examination staff years used in FY 2001. The actual shift of resources in FY 2002 will depend on the timing and volume of determination application receipts.



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**Project Management Techniques  
Should Be Used to Effectively  
Implement the Determination  
Letter Strategy**

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provided with the application and those that need further review by an EP revenue agent. In anticipation of the increase in applications, the strategy includes establishing up to six additional screening sites throughout the country in order to minimize any backlogs at the screening level.

This commitment is commensurate with the TE/GE Division's belief that the determination letter program is the IRS' key link to the employee benefits plan community. The IRS, through the determination letter program, informs employers if their plan formats comply with the current laws, essentially protecting millions of participating employees from unintended tax consequences.

Although TE/GE management developed a strategy to prepare for the peak determination letter workload, additional efforts are needed to ensure that potentially critical issues are prominently in the view of TE/GE management. If issues are not resolved as they occur, there is a risk that events could hamper the TE/GE Division's ability to effectively implement the overall strategy, which focuses on timely issuing determination letters and maintaining good customer service. If determination letters are delayed, it could result in increased burden on employers that are waiting for a determination on their employee plans.

The TE/GE Division's strategy did not include a structured project management approach to coordinate, monitor, or report on the actions in process by all the various functions involved with implementing the strategy. Instead, TE/GE management used conference calls and status meetings to discuss the actions needed to prepare for the peak receipt period. However, because there were no overall lists of completed tasks, outstanding items, or risks identified, TE/GE management did not have a tool that tracked the readiness of all aspects of the strategy. This made it difficult to know whether the TE/GE Division would be ready to handle the increased workload when the peak period began, as well as to identify new risks as the strategy unfolds.

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To illustrate the effects of not using a structured management approach, we cite three examples where risks had not been timely or completely resolved prior to December 31, 2001, the original date for the beginning of the peak period.

**Formal notification of process changes to the employees' union**

As the application screening and assignment strategy was being developed by the TE/GE Division, a labor relations specialist advised that the impact of modifying some revenue agents' work assignments<sup>8</sup> warranted a formal notification to the IRS employees' union under the labor/management bargaining provisions. TE/GE management initially considered this and had preliminary contacts with union representatives regarding the strategy and the change in work assignments. In September 2001, they decided it was not necessary to pursue the formal concurrence of the employees' union. However, subsequent to this decision, as the peak receipt period neared, other TE/GE officials indicated they thought a formal notification to the employees' union was still being planned. At the time of our review, it was not clear if TE/GE management had completely resolved whether a formal notification was warranted. Processing delays could occur if formal negotiations become necessary during the peak period.

**Capacity of the automated determination letter processing system**

The TE/GE Division's FY 2002 Strategic Plan indicated that a redesign<sup>9</sup> of the current automated determination

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<sup>8</sup> In general, the work assignment modifications involve assigning agents to screen determination applications who had previously been doing detailed reviews of applications, and assigning agents to do detailed reviews of applications who had previously been doing examinations of the operational compliance of plans.

<sup>9</sup> The project to redesign the TE/GE Division's current automated determination letter processing system has been delayed and is not expected to offer any system improvements in FY 2002.

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letter processing system was necessary to avoid downtime and delays because the system was stretched beyond its capacity. The TE/GE Division's strategy for processing the increased volume of applications may aggravate this condition since many employees may be shifted to the determination program, which will increase the number of potential system users. For example, one of the system constraints was a limit of 250 simultaneously logged-on users. System administrators told us that the system was already approaching the 250-user limit before the peak period began and that approximately 245 new user profiles were added between July 1, 2001, and January 16, 2002. The TE/GE Division indicated that a contingency plan would be to stagger the users' access to the system, if necessary.

As the peak receipt period neared, it was not clear if TE/GE management had completely resolved whether system issues could limit the effectiveness of the workload distribution strategy. If the new users attempt to log-on to the system along with the regular users, the system limit may be exceeded and the TE/GE Division will have to address system problems sooner than planned. Processing delays could occur if all the anticipated users cannot efficiently access the system or if the responsiveness of system access is significantly degraded because of an increase in users.

**Resources for the initial processing of applications**

The TE/GE Division's Business Performance Review indicated that the higher volumes of applications will require additional resources to maintain the timeliness of the IRS' initial clerical processing of determination letter applications, which is done by the Small Business/Self-Employed (SB/SE) Division Submission Processing Center staff. The TE/GE Division and the SB/SE Division estimated that 50 additional staff years above the historical base of 30 staff years would be required for FY 2002. As the peak receipt period neared, the SB/SE Division was still in the process of recruiting and hiring additional employees for the higher volume of determination work expected and had not yet received additional computer terminals that had

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been ordered. The TE/GE Division indicated that, historically, the processing center has been able to take steps to handle resource issues, when necessary.

It was not clear if TE/GE management had completely resolved whether the SB/SE Division's level of readiness would create bottlenecks if large volumes were actually received at the deadline date and the hiring and training had not been completed. The IRS subsequently extended the date for the end of the remedial period, which also gave the IRS additional time to hire staff and obtain equipment.

**Project management techniques would help**

One of the standards for effective internal control in government<sup>10</sup> is that management should identify and analyze risks associated with achieving their objectives. Methods for doing this vary, so management must select an appropriate way to manage risks.

We believe that project management techniques would have helped all levels of TE/GE management review what issues exist and assess if associated risks have been addressed to their satisfaction. A structured approach would also help highlight issues for management attention throughout the duration of the strategy. Project management is defining, planning, scheduling, and controlling the tasks that must be completed to accomplish project goals. Project management techniques can help organize the details of a project by listing tasks or action items to be accomplished, setting schedule or milestone dates, having regular progress reviews, and listing any changes that need to be made or issues that need action. Using these tools normally requires that a project manager or team leader be designated. While TE/GE management used some of these techniques, they did not formally designate a project manager to ensure that project management techniques are applied throughout the implementation of the strategy.

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<sup>10</sup> Standards for Internal Control in the Federal Government (GAO/AIMD-00-21.3.1, November 1999).

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The TE/GE Division acknowledges that peak receipt periods make it exceptionally difficult to maintain good customer service. Employers suffer additional burdens as the time frame for receiving their determination letters lengthens. Timely responses are important. If the changes to the benefit plans as a result of the GUST are incomplete or incorrect, a prompt determination from the IRS will enable the employer to make the necessary corrections as quickly as possible. This has downstream impacts on the IRS as well, because it must dedicate more resources to respond to customers inquiring about the status of their determination application.

Individuals, organizations, and the public at large rely on the IRS to ensure that employee benefit plans follow the complex tax laws and guidance that regulate their operations. The IRS' effectiveness in providing prompt customer service in the determination letter area helps in maintaining public confidence and fairness in tax administration.

**Recommendation**

1. The Commissioner, TE/GE Division, should designate a manager to assume the responsibility of using appropriate project management techniques as soon as possible and for the duration of the EP determination letter strategy (through FYs 2002 and 2003, or until the volume of applications returns to normal levels).

Management's Response: The Director, EP function, appointed a manager to assume program responsibility and apply project management techniques for the increase in the determination letter workload.

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**Appendix I**

**Detailed Objective, Scope, and Methodology**

The overall objective of this review was to determine if potential risks to the implementation of the employee plans determination letter strategy are being effectively addressed by the Tax Exempt and Government Entities (TE/GE) Division. To accomplish this objective, we:

- I. Determined if there were unresolved readiness issues pertaining to the TE/GE Division's Employee Plans (EP) determination letter strategy.
  - A. Reviewed the draft versions of the TE/GE Division's Fiscal Year (FY) 2002-2003 Strategic Assessment, FY 2002-2003 Strategy and Program Plans, FY 2002 EP Work Plan, and Business Performance Review.
  - B. Reviewed other available documents that communicated the determination letter strategy, such as management slide-show presentations, memoranda, TE/GE Division newsletters, and Internal Revenue Service (IRS) notices and announcements.
  - C. Interviewed TE/GE Division personnel responsible for selected segments of the strategy to gauge the level of readiness to implement the strategy. As applicable, interviewed personnel of other IRS functions where activities were relevant to the EP strategy (Information Technology Services, Small Business/Self-Employed Submission Processing, and Statistics of Income).
  - D. Evaluated the status of major segments in the strategy and identified incomplete tasks or unresolved problems that appeared to have the potential to adversely impact the strategy if not timely addressed.
- II. Determined if management oversight appeared effective in identifying significant issues and ensuring that action items were monitored.
  - A. Interviewed TE/GE management personnel to determine if an overall issue owner or project leader had been designated to coordinate the strategy's implementation or if there were written implementation plans that included all the functions that have a role in processing the determination letter applications.
  - B. Discussed unresolved issues and the related potential risks with EP management to determine their roles in providing oversight to the strategy.

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**Appendix II**

**Major Contributors to This Report**

Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)

Joseph W. Edwards, Director

Nancy A. Nakamura, Director

Ronald F. Koperniak, Audit Manager

Timothy A. Chriest, Senior Auditor

Janice A. Murphy, Senior Auditor

Joseph P. Snyder, Senior Auditor

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**Appendix III**

**Report Distribution List**

Commissioner N:C  
Deputy Commissioner, Tax Exempt and Government Entities Division T  
Director, Employee Plans, Tax Exempt and Government Entities Division T:EP  
Director, Rulings and Agreements, Tax Exempt and Government Entities Division T:EP:RA  
Manager, Employee Plans Determinations, Tax Exempt and Government Entities Division  
T:EP:RA:D  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O  
Office of Management Controls N:CFO:F:M  
Audit Liaisons:  
Commissioner, Small Business/Self-Employed Division S:COM  
Director, Communications and Liaison, Tax Exempt and Government Entities  
Division T:CL



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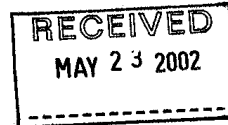
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**Appendix IV**

**Management's Response to the Draft Report**

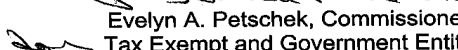


DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224



MAY 17 2002

**MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT**

**FROM:**  Evelyn A. Petschek, Commissioner  
Tax Exempt and Government Entities Division

**SUBJECT:** Management Advisory Report: (Audit #200110050)  
Project Management Techniques Would Help in  
Managing Risks for The Increased Employee Plan  
Determination Letter Workload

I reviewed your draft report on the way the Employee Plans Division designed a multifaceted strategy to continue to provide top-quality service to its customers during the expected peak in the determination letter application workload.

Our strategy reflects a high level of commitment to minimizing any detrimental impact on customer satisfaction or customer burden that might be caused if the increased number of applications caused a delay in processing determination letter requests.

Our comments on your recommendation follow:

**RECOMMENDATION:**

The Commissioner, TE/GE Division, should designate a manager to assume the responsibility of using appropriate project management techniques as soon as possible and for the duration of the EP determination letter strategy (through FYs 2002 and 2003, or until the volume of applications returns to normal levels).

**ASSESSMENT OF CAUSE**

TIGTA observed that project management techniques would help all levels of TE/GE management identify and resolve the issues and associated risks arising from the projected increase in employee plans determination letter workload. TIGTA further observed that using project management techniques normally requires the appointment of a project manager or team leader.

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CORRECTIVE ACTION: Completed

The Director, Employee Plans appointed a manager to assume program responsibility and apply project management techniques for the increase in the employee plans determination letter workload.

IMPLEMENTATION DATE: Completed

RESPONSIBLE OFFICIAL: Completed

CORRECTIVE ACTION MONITORING PLAN: Completed